BEFORE

THE PUBLIC SERVICE COMMISSION OF

SOUTH CAROLINA

DOCKET NO. 2019-290-WS

IN RE:	)	**RESPONSE OF SOUTH CAROLINA DEPARTMENT OF CONSUMER AFFAIRS TO BLUE GRANITE WATER COMPANY'S PETITION FOR RECONSIDERATION AND CLARIFICATION**
	)	
Application of Blue Granite Water Company for Approval to Adjust Its Rate Schedules and Increase Rates	))))	

The South Carolina Department of Consumer Affairs ("Department") submits this response to Blue Granite Water Company's ("Blue Granite") Petition for Reconsideration and Rehearing of Order No. 2020-306 ("Petition"). To the extent the Petition seeks reconsideration of the 7.46% Return on Equity ("ROE", also referred to as "cost of equity") authorized in the Order, the Public Service Commission ("Commission") should deny the Petition.

I. Introduction.

Blue Granite contends the Commission's Order is arbitrary and capricious because there is no evidence in the record to support the finding that the ROE meets the requirements of *Federal Power Commission v. Hope Natural Gas Company*, 320 U.S. 591 (1942), and *Bluefield Water Works & Improvement Company v. Public Service Commission of West Virginia*, 262 U.S. 679 (1923). As Blue Granite notes, three witnesses, one each for the company, the Office of Regulatory Staff ("ORS"), and the Department, submitted testimony regarding the ROE. These three experts applied a variety of models to proxy groups of companies, relying on comparable data from those companies, as well as their expert opinions, to produce a range of recommendations that would meet the requirements of *Hope* and *Bluefield*. This is the same exercise performed by all ROE experts testifying before the Commission and is a well-established component of utility ratemaking.

The experts did not rely on any one model to determine a ROE, but rather each provided modeling results, along with their subjective adjustments, as guidelines for the Commission to consider in determining the ROE for Blue Granite. None of the experts used an identical set of models or adjustments to prepare their respective recommendations.[1] As the Commission correctly notes in its Order, it has the responsibility to weigh the testimony and evidence and draw "the ultimate conclusion therefrom as to what return is necessary to enable a utility to attract capital . . . .because the Commission is a body of experts 'composed of men of special knowledge, observation, and experience' in the field of rate regulation." *State ex rel. Utilities Com. v. General Tel. Co*., 281 N.C. 318, 371 (1972); *see also, S. Bell Tel. & Tel. Co. v. Pub. Serv. Comm'n*, 270 S.C. 590, 597(1978). "The right to weigh the evidence submitted is peculiarly within the Commission's province. Evidence should be believed unless there is some reason for discrediting it." *S. Bell Tel. & Tel. Co. v. Pub. Serv. Comm'n*, 270 S.C. 590, 598 (1978).

II. Witness Rothchild's Recommendations Support the Commission's Order

It is evident from the record and Order that the Commission gave substantial consideration to each of the experts' models and opinions. Department witness Rothschild provided approximately 100 pages of pre-filed direct and surrebuttal testimony, not including exhibits. The Commission notes it found Rothschild "credible, compelling, unbiased and without prejudice in balancing the interests of the consumer and the utility…" (Order, at p. 126). As indicated in his

[1] "All three ROE witnesses arrived at their recommended rates and ranges of rates by applying common equity models including Constant Growth Discounted Cash Flow ("DCF") and Capital Asset Pricing Model ("CAPM"). Tr. p. 541.2, p. 661.5, p. 1000.3-1000.4. Witness D'Ascendis also utilized Empirical Capital Asset Pricing Model ("ECAPM") and the Risk Premium Model ("RPM"). Tr. p. 541.2. ORS witness Parcell's additional model included the Comparable Earnings Model ("CEM"). Tr. pp. 1000.3-1000.4. Consumer Affairs witness Rothschild included the Non-Constant DCF method as his third approach. Tr. p. 661.5." (Order, at p. 39)

testimony and shown in the table below, the high-end results of Rothschild's three ROE (or cost of equity) models range between 6.96% and 9.68%, averaging 8.75%, while the low-end results of the models range between 5.72% and 8.34%, averaging 7.46%. (Tr. at pp. 672.8-672.9).

TABLE 4: Cost of Equity Model Results

	Low	High
DCF - CONSTANT GROWTH	8.34%	8.76%
DCF - NON-CONSTANT GROWTH	5.72%	6.96%
CAPM		
Risk Free Rate - 3-Month T Bill	7.76%	9.59%
Risk Free Rate - 30-yr T Bond	8.02%	9.68%
Range	7.46%	8.75%

Source: Schedule ALR 2

In his pre-filed testimony, Rothschild did emphasize an 8.65% ROE for Blue Granite; however, upon questioning by the Commission at the hearing, it was clear that the ranges provided by his models were considered reasonable in his opinion. The following is an excerpt of the Commission's questioning of Mr. Rothschild:

> Q Mr. Rothschild, is there any particular reason that you recommended point estimates for the company's ROE and cost of capital rather than the interval estimate?
> A (ROTHSCHILD) Why did I recommend 8.65 instead of -- instead of a range?
> Q Yeah.
> A (ROTHSCHILD) I have -- I've -- sometimes in testimonies, I've provided ranges if that's helpful, and often people have asked for something precise. That -- that is the number that I came up to based on my analysis, and I show the justification. I appreciate your question, because to assume that -- that this exercise is that precise is an excellent question, so I think you generally can't say it's 8.65 or 8.61. So there are various ranges that I do show in my testimony that I hope would help understand a range that's reasonable.
>
> (Tr. at p. 720).
>
> In his surrebuttal testimony, Rothschild explains:
>
> "As with other tools and methodologies we use regularly, option- implied betas are not a silver bullet and should be used in conjunction with other valid approaches to determine ranges of reasonableness for the cost of equity. The more

valid tools we use, the more we can narrow down or confirm these ranges of reasonableness to ensure a more accurate result." (Tr. at p. 683.19)

As detailed above, the ROE range Rothschild presented to the Commission in his direct testimony and during the hearing was 7.46% to 8.75%. Notably, he ends his pre-filed surrebuttal testimony by stating, "If adopted, my cost recommendations would allow BGWC to raise the capital it needs to provide safe and reliable service because my recommendations are consistent with investors' return expectations." (Tr. at p. 683.26). Additionally, when providing a summary of his testimony at the hearing, Rothschild stated "[m]y recommendations satisfy the requirements of Hope and Bluefield that regulated utility companies should have an opportunity to earn a return commensurate with returns on investments in other enterprises having corresponding risks." (Tr. at pp. 661-662).

In the Petition, Blue Granite notes the *Bluefield* factors that require the Commission to set a rate of return "equal to that generally being earned at the same time and in the same general part of the country on investments in other business undertakings which are attended by similar risks and uncertainties, *including non-utility investments*." (Petition, at p.4) (Emphasis added). While it may benefit Blue Granite to include "non-utility investments" in the ROE analysis as its witness Mr. D'Ascendis did, this is not a requirement of *Bluefield*.[2]

In fact, of particular concern to the Commission was D'Ascendis' inclusion of fourteen (14) non-price regulated, non-utility companies[3] in his proxy groups. D'Ascendis was the only witness to use a non-price regulated, non-utility proxy group in his models and both ORS witness

[2] *Bluefield* holds "[a] public utility is entitled to such rates as will permit it to earn a return on the value of the property it employs for the convenience of the public equal to that generally being made at the same time and in the same region of the country on investments in other business undertakings which are attended by corresponding risks and uncertainties…" (*Bluefield*, 262 U.S. at 692).

[3] Among others, the companies included AutoZone, Cracker Barrel, Cheesecake Factory, and Dollar General. See Transcript at p. 615 and Hearing Exhibit 16 (D'Ascendis Direct Exhibit No. 1 Schedule DWD-6).

Parcell and Department witness Rothschild criticized the inclusion of these companies. Noting D'Ascendis' "NonPrice Regulated Group indicated an average unadjusted beta that is twenty-five percent (25%) higher than his Water Proxy Group…", the Commission properly found the non-utility companies used in D'Ascendis' models did not possess similar risks and uncertainties to Blue Granite and therefore, were not appropriate for comparison. (Order, at pp. 41 and 42). The Commission agreed with witnesses Rothschild and Parcell that the use of non-price regulated, non-utility companies greatly influenced D'Ascendis' models and, as a result, his ROE recommendations (9.75% to 10.25%) were too high.[4] (Order, at p. 38).

III. Conclusion

As noted in the Petition, only three experts testified regarding ROE. Weighing the testimony, the Commission found the Department's expert the most credible and it discredited the evidence and testimony of Blue Granite's ROE witness. Further, the Commission is not bound by the opinion of any one expert as the Commissioners themselves are considered to be experts in utility ratemaking, able to deduct from the testimony a reasonable ROE. The testimonies and Order provide substantial evidence to support the Commission's conclusions. Therefore, to the extent the Petition seeks reconsideration of the 7.46% ROE, it should be denied.

Respectfully submitted,

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[4] D'Ascendis' DCF results indicated an average ROE for his proxy water group of 8.91% and Rothschild's DCF-Constant Growth ranges for his proxy water group were 8.34% to 8.76%. Also note, the DCF Model used by D'Ascendis resulted in Indicated Common Equity Cost Rates of 6.75% and 6.78% for two of the companies in his proxy water group. (See Hearing Exhibit 17, p. 3 of 33).